



# Macroeconomic Policies and Growth: Expectations, Structural Realities, and Theoretical Weaknesses

NNANU, Friday Ben; \*GOBIR, Mustapha Abdullahi Ph.D and YEIH, Waamene

Department of Economics, University of Abuja, Nigeria

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\*Corresponding Author: GOBIR, Mustapha Abdullahi Ph.D

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## Abstract

## Original Research Article

This article evaluates how macroeconomic policies shape long-term economic growth when viewed through the lens of foundational and contemporary growth theories. It analyzes the core tenets, policy expectations, and fundamental weaknesses of these theoretical frameworks when applied to real-world macroeconomic management, with a specific focus on developing regions like Nigeria. By reviewing resource-based, export-led, Schumpeterian, structuralist dual-economy, classical stage-based, Harrod-Domar, neoclassical, and endogenous growth models, this paper uncovers a deep disconnect between abstract theoretical assumptions and empirical realities. Our analysis reveals that while growth theories offer essential blueprints for fiscal, monetary, and trade policies, their execution in developing countries is routinely undermined by weak institutions, Dutch Disease dynamics, volatile commodity markets, structural rigidities, and missing domestic value chains. The study concludes that sustainable economic growth cannot be achieved by blindly adhering to a single growth model. Instead, it requires a flexible, structurally adaptive macroeconomic policy mix that pairs targeted industrial strategies with institutional reforms, technological accumulation, and genuine economic diversification.

**Keywords:** Macroeconomic Policy, Growth Theory, Structural Rigidities, Resource Curse, Technological Innovation, Developing Economies.

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## 1. Introduction

### 1.1 Background to the Study

At its core, the ultimate goal of macroeconomic policy is to build and sustain an economic environment that fosters robust, inclusive, and ecologically sustainable long-term growth. Achieving this goal is what allows developing and emerging economies to close the per capita income gap with advanced nations, lifting millions out of poverty and raising everyday living standards. Historically, the speed and

endurance of economic growth depend heavily on the quality, consistency, and structural alignment of a country's macroeconomic policy mix. Both institutional assessments (International Monetary Fund [IMF], 2021) and foundational empirical literature (World Bank, 2022) demonstrate that sound, steady macroeconomic policies are strongly tied to accelerated economic growth.

Within standard macroeconomic frameworks, a growth-supportive policy environment stands on five key pillars:



- A low, stable, and predictable inflation rate.
- An appropriate real interest rate structure that encourages investment.
- A stable, sustainable, and countercyclical fiscal trajectory.
- A competitive, transparent, and predictable real exchange rate regime.
- A viable, shock-resilient balance of payments position.

Countries that successfully align these variables generally enjoy higher rates of capital accumulation and improvements in total factor productivity (TFP). However, global economic history shows that satisfying only one or two of these conditions rarely sustains momentum. Furthermore, the direction of cause and effect is complex: while stable macroeconomic conditions spark growth, strong economic growth gives policymakers the fiscal space and monetary flexibility they need to maintain that very stability (Onyeiwu, 2021).

This paper offers a critical look at both the theoretical designs and real-world outcomes of macroeconomic policy models. Because fiscal and monetary choices directly drive inflation, exchange rate paths, and public capital investments, understanding how these policies intersect with long-term growth theory is critical. Ultimately, macroeconomic policy must balance short-run stabilization—like smoothing out business cycles—with long-run structural transformation (Ajakaiye and Olaniyan, 2021).

## 1.2 Statement of the Problem

In the pursuit of sustained economic growth, both advanced and developing nations build their fiscal, monetary, and trade policies around the explicit promises of various economic growth theories. Yet, the actual macroeconomic performance of many developing countries—particularly in Sub-Saharan Africa—over the past several decades has been highly volatile, uneven, and disappointing. This stagnation is frequently marked by low domestic savings, volatile investment trends, structural fiscal deficits, and chronic external trade imbalances

(Apata, 2024).

Nigeria provides a clear example of this disconnect between theory and reality. Following the global recovery in 2021, crude oil prices surged well above \$120 per barrel. According to traditional resource-based or classical export-led growth models, this windfall should have translated into massive fiscal surpluses, robust foreign exchange reserves, monetary stability, and rapid domestic economic expansion. Instead, the Nigerian economy faced disappointing net oil revenues due to production shortfalls and fiscal leakages, a volatile foreign exchange market, a weak balance of payments position, and stubborn inflationary pressures (Obi, 2023).

Data from the National Bureau of Statistics (NBS, 2023) shows that while real Gross Domestic Product (GDP) growth rose from 0.15% in Q1 2021 to 5.01% in Q2 2021, it quickly lost steam, dropping to 2.25% by Q3 2022. This deceleration occurred despite a flurry of monetary interventions and fiscal adjustments by authorities.

This persistent gap raises critical macroeconomic questions:

- Why is there such a recurring disconnect between the optimistic predictions of growth theories and the actual outcomes of macroeconomic policies in developing nations?
- What are the underlying structural weaknesses of these theories when we try to turn them into practical policy tools?
- How do institutional failures, market frictions, and global structural inequalities undermine the transmission of fiscal and monetary instruments?

## 1.3 Objectives of the Study

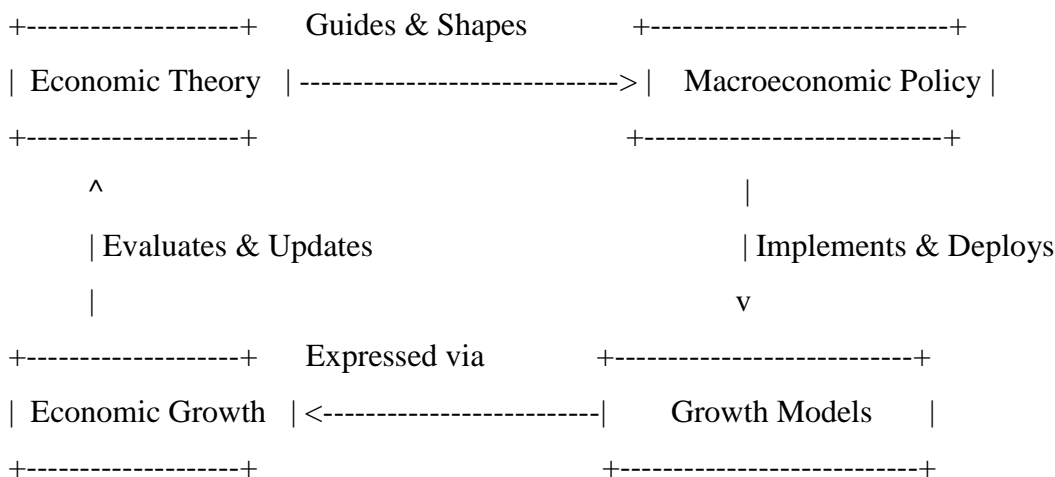
The primary objective of this study is to analyze prominent economic growth theories, evaluating their policy expectations, structural limitations, and suitability for building effective macroeconomic frameworks.

The specific objectives are to:

- Review the foundational mechanisms and policy assertions of major economic growth theories.
- Unpack the macroeconomic policy expectations derived from these theoretical models.
- Identify and analyze the structural weaknesses that limit these growth theories from delivering sustainable economic growth in developing countries.
- Offer strategic, structurally adaptive macroeconomic policy recommendations to help bridge the gap between growth theory and empirical reality.

## 2. Conceptual Review

To establish a clear analytical foundation, it is necessary to define the core concepts that connect theoretical design with applied macroeconomic management.



### 2.1 Economic Theory

Economic theory is a logically consistent set of ideas, principles, and mathematical frameworks designed to explain how economic agents, markets, and aggregate systems behave (Mankiw, 2021). It serves as an analytical lens that allows researchers and policymakers to diagnose economic challenges, project future outcomes, and evaluate alternative policy options. By simplifying complex realities into isolated variables, economic theories provide the structural rules needed to test hypotheses and understand how changes in fiscal, monetary, institutional, or technological parameters impact societal welfare and production.

### 2.2 Macroeconomic Policy

Macroeconomic policy refers to the strategic interventions, regulations, and instruments deployed by fiscal authorities (governments) and monetary authorities (central banks) to steer an economy’s aggregate performance (Blanchard, 2021). Operating primarily through fiscal mechanisms (taxation, public spending, and debt management) and monetary mechanisms (interest rates, open market operations, reserve requirements, and exchange rate interventions), its core objectives include price stability, full employment, external balance, and sustainable economic output. These policies can be configured as countercyclical, procyclical, expansionary, or contractionary, depending on

short-run stability needs and long-run structural targets.

## 2.3 Economic Growth

Economic growth is the sustained, long-term increase in an economy's capacity to produce and distribute goods and services, typically measured by the annualized percentage change in real Gross Domestic Product (GDP) or real per capita income (Acemoglu, 2020). Unlike short-run economic stabilization, which focuses on managing demand-side fluctuations around a trend, long-run economic growth concerns the expansion of the economy's supply capacity. This expansion depends on the accumulation of physical capital, labor force growth, human capital development, institutional quality, and total factor productivity (TFP) improvements driven by technological progress (Todaro & Smith, 2020).

## 2.4 Models of Economic Growth

Because real-world economies are driven by a complex, evolving mix of factors, growth models employ mathematical and logical simplifications to isolate and aggregate the primary drivers of long-run output. Growth models are generally categorized by their temporal and structural assumptions (Woźniak-Jęchorek, 2022). Long-term models map out steady-state paths to identify how capital, labor, and technology interact over time. In classical and early neoclassical iterations, parameters like population growth, labor supply, and depreciation rates are treated as exogenously determined, whereas savings and investment rates vary across different models, serving as either fixed parameters or endogenous choices.

## 3. Methodology

This study adopts a qualitative, analytical methodology grounded in critical conceptual evaluation and comparative theoretical analysis. Rather than testing a single empirical dataset, the paper systematically reviews the structural assumptions, policy architectures, and behavioral mechanisms embedded in major

historical and contemporary economic growth models.

The analytical process involves:

- Tracking the historical and mathematical evolution of each model.
- Grouping their core assertions regarding how macroeconomic policy tools (such as public capital expenditure, interest rates, tariffs, and exchange rates) impact output.
- Conducting a structural critique of each theory's assumptions against the realities of developing economies, highlighting institutional gaps, structural rigidities, and asymmetric global market dynamics.

## 4. Analysis of Growth Theories: Expectations, Weaknesses, and Policy Frameworks

### 4.1 Resource-Based Growth Theory

#### 4.1.1 Theoretical Framework and Core Tenets

Resource-Based Growth Theory argues that natural resource endowments—such as oil, natural gas, solid minerals, and fertile agricultural land—serve as primary catalysts for capital accumulation and economic development. The model assumes that countries rich in natural resources can bypass early domestic savings constraints by extracting and exporting these endowments. This extraction generates the foreign exchange and fiscal revenues needed to import capital equipment, build infrastructure, and fund public services.

The theoretical foundation dates back to Harold Hotelling's seminal work, which mathematically demonstrated that the optimal extraction path of a non-renewable resource depends on the asset's capital appreciation relative to the prevailing market interest rate. This concept is captured in the Hotelling Rule:

$$\frac{\dot{p}_t}{p_t} = r$$

where  $p_t$  represents the net price (rent) of the resource at time 't',  $\dot{p}_t$  is its time derivative, and 'r' is the nominal interest rate. This framework treats natural resources as a form of natural capital that can be converted into physical or

human capital to support long-term development. Mid-twentieth-century structuralists later expanded on this, discussing how resource extraction could generate upstream and downstream industrial linkages across the wider economy.

#### 4.1.2 Macroeconomic Policy Expectations

- **Fiscal Revenue Generation:** Large-scale extraction produces substantial economic rents (royalties, corporate taxes, production-sharing agreements), offering governments a broad tax base independent of heavy domestic taxation.
- **Foreign Exchange Inflows:** Resource exports generate consistent hard currency inflows, relaxing external balance-of-payments constraints and allowing the country to import advanced industrial machinery.
- **Infrastructure Catalyst:** The initial capital requirements for resource extraction (ports, rail networks, power grids) are expected to create positive infrastructure spillovers for other domestic sectors.

#### 4.1.3 Theoretical and Structural Weaknesses

- **The Resource Curse and Institutional Degradation:** Contemporary empirical work (Ross, 2020) demonstrates that abundant natural resources often correlate with slower economic growth and political instability. The

concentration of wealth within extraction enclaves encourages rent-seeking behavior, deepens systemic corruption, and weakens broad-based institutional quality.

- **Dutch Disease Dynamics:** Large resource export windfalls appreciate the nation's Real Effective Exchange Rate (REER). This appreciation reduces the international competitiveness of non-resource tradable sectors, such as manufacturing and agriculture, leading to structural deindustrialization (Etim & Edet, 2021).
- **Commodity Price Volatility:** Reliance on primary resource exports exposes the macroeconomy to intense global price cycles. This volatility leads to procyclical fiscal policy, where public spending spikes during booms and collapses during busts, disrupting long-term development planning (World Bank, 2022).
- **Finite Depletion:** Exhaustible resources face inevitable depletion. Without an active strategy to convert resource revenues into reproducible assets, long-run growth paths remain unsustainable.

#### 4.1.4 Macroeconomic Policy Matrix

To mitigate these structural vulnerabilities, the theory requires specific macroeconomic policy adjustments:

Policy Domain	Recommended Instrument	Structural Objective
Fiscal Policy	Sovereign Wealth Funds (SWFs) & Fiscal Rules	To save windfall revenues, insulate public spending from commodity cycles, and ensure intergenerational equity.

Policy Domain	Recommended Instrument	Structural Objective
Monetary Policy	Sterilization Operations & Managed Floating REER	To counteract domestic liquidity surges from resource inflows and protect the competitiveness of non-resource exports.
Structural Policy	Strategic Diversification Incentives	Using resource revenues to subsidize industrial zones, human capital, and agricultural processing.

## 4.2 Export-Led Growth (ELG) Theory

### 4.2.1 Theoretical Framework and Core Tenets

Export-Led Growth Theory asserts that a country’s long-term growth trajectory is primarily driven by expanding its export capacity, particularly in manufactured and high-value-added goods. Unlike import-substitution industrialization (ISI), which focuses on constrained domestic markets, ELG targets global demand. This approach allows domestic firms to capture economies of scale, gain exposure to international competition, and access foreign technologies (Krugman *et al.*, 2022).

### 4.2.2 Macroeconomic Policy Expectations

- **Overcoming Domestic Demand Constraints:** Small or low-income economies can bypass limited domestic purchasing power by tapping into global consumer markets.
- **Efficiency Gains via Global Competition:** Exposure to international markets forces domestic firms to minimize waste, optimize production processes, and upgrade product quality.
- **Learning-by-Exporting Spillovers:** Engaging with international buyers encourages rapid technology transfers, knowledge sharing, and managerial skill development that spread to non-exporting sectors.

- **Hard Currency Accumulation:** Sustained export surpluses build foreign exchange reserves, reducing vulnerability to sudden stop capital flight and balance-of-payments shocks.

### 4.2.3 Theoretical and Structural Weaknesses

- **The Prebisch-Singer Hypothesis:** Developing countries that export primary or low-processed goods while importing advanced manufactured commodities face a long-term decline in their terms of trade (TOT), defined as:

$$TOT = \frac{Px}{Pm}$$

where Px is the aggregate index of export prices and Pm is the aggregate index of import prices. Over time, income elasticity of demand for manufactured goods outpaces that for primary products, causing primary exporters to export larger volumes just to maintain a constant volume of imports (Oyekale, 2022).

- **Fallacy of Composition:** If multiple developing countries simultaneously implement ELG strategies by exporting similar low-skill, labor-intensive products, they risk oversaturating global markets. This collective overproduction drives down world prices, eroding profit margins for all participating nations.
- **External Vulnerability:** High export-to-GDP ratios expose the domestic economy to external demand shocks,

shifts in global trade policy, and protectionist measures in advanced consumer nations.

- **Internal Enclave Development:** Export production zones can turn into isolated economic enclaves that lack deep

backward and forward integration with the domestic economy.

#### 4.2.4 Macroeconomic Policy Matrix

To align ELG expectations with structural realities, the following framework is required:

Policy Domain	Recommended Instrument	Structural Objective
Exchange Rate Policy	Competitive Exchange Management      Real Rate	Maintaining an undervalued or highly stable real exchange rate to support the price competitiveness of exports.
Trade & Fiscal Policy	Export Subsidies, Duty Drawback Schemes, and SEZs	Lowering input costs for exporters, establishing Special Economic Zones (SEZs), and removing regulatory friction at ports.
Industrial Policy	Targeted R&D & Tech-Upgrading Grants	Supporting transition from low-tech primary processing to complex, high-value manufactured goods.

### 4.3 Schumpeterian Theory of Economic Growth

#### 4.3.1 Theoretical Framework and Core Tenets

Joseph Schumpeter's growth model places the entrepreneur and technological innovation at the center of economic development. Schumpeter argued that economic growth is not a smooth, gradual accumulation of capital and labor. Instead, it is a dynamic process driven by discontinuous, disruptive qualitative transformations. The core engine of this model is Creative Destruction, where new innovations constantly displace outmoded production methodologies, market structures, and technologies (Aghion *et al.*, 2021).

Schumpeter defined five distinct forms of innovation:

1. Introduction of a new good or qualitative grade of a good.
2. Implementation of a new production method.
3. Opening of a new consumer or input market.
4. Acquisition of a new supply source for raw materials.
5. Reorganization of an industry structure (e.g., breaking or creating monopolies).

The Schumpeterian aggregate production function can be formulated as:

$$Q=f(K, R, L, F, W)$$

where Q represents aggregate output, K is physical capital ("produced means of

production"), R represents natural resources, L is the employed labor force, F represents the society's inventory of technical knowledge, and W reflects the institutional, socio-cultural, and regulatory environment. Growth accelerates when changes in F and W disrupt existing equilibria, opening up new opportunities for capital accumulation funded by credit creation.

#### 4.3.2 Macroeconomic Policy Expectations

- **Productivity Frontiers:** Continuous innovation drives sustained shifts in total factor productivity (TFP), preventing the economy from hitting the diminishing marginal returns to capital characteristic of static models.
- **Endogenous Business Cycles:** Innovation clusters generate structural investment waves that drive expansionary cycles, while the obsolescence of older industries creates healthy, reallocative recessions.
- **Capital Accumulation Driven by Profit Incentives:** Successful innovators secure temporary monopoly profits, providing strong incentives for private research and development (R&D) investments.

#### 4.3.3 Theoretical and Structural Weaknesses

- **Assumption of Deep, Functioning Credit Markets:** The Schumpeterian

framework assumes advanced financial institutions can evaluate risk and extend credit to unproven entrepreneurs. In many developing nations, credit markets suffer from high collateral requirements and risk aversion, often prioritizing short-term government debt over long-term industrial innovation (Okunlola *et al.*, 2022).

- **Disregard for Structural Displacements:** Creative destruction can cause significant short- to medium-run welfare losses. It can lead to structural unemployment, plant closures, and regional declines that require robust social safety nets.
- **Monopolistic Market Distortions:** Left unregulated, the temporary monopolies granted to successful innovators can turn into permanent, anti-competitive market structures. These entrenched monopolies can buy up potential competitors and actively suppress subsequent innovation waves.
- **Institutional and Technical Bottlenecks:** Developing countries often lack the baseline human capital, intellectual property protections, and physical infrastructure needed to generate frontier innovations, making them reliant on costly foreign technology imports (Olugbire *et al.*, 2023).

#### 4.3.4 Macroeconomic Policy Matrix

SCHUMPETERIAN POLICY MIX		
v	v	v
Monetary / Financial	Fiscal / Industrial	Structural / Legal
- Innovation Credits	- R&D Tax Offsets	- Patent Protections
- Venture Capital Seed	- STEM Grants	- Anti-Monopoly Rules

- Monetary & Financial Policy:** Developing dedicated innovation credit windows, venture capital matching funds, and specialized development bank structures to derisk lending to early-stage technology enterprises.
- Fiscal & Industrial Policy:** Implementing R&D tax credits, funding public research institutes, and offering educational grants to build a domestic workforce strong in science, technology, engineering, and mathematics (STEM).
- Structural & Regulatory Policy:** Updating intellectual property laws to balance rewarding innovators with ensuring fair market competition, alongside antitrust frameworks to prevent incumbent market dominance.

#### 4.4 Synthesis: Structuralist, Classical Stage, Harrod-Domar, Neoclassical, and Endogenous Growth Theories

To provide a comprehensive overview of how macroeconomic policies intersect with the broader landscape of growth theory, we must

analyze the progression from early structural models to contemporary endogenous frameworks.

##### 4.4.1 Dual-Economy Growth Model (Lewis, 1954)

- Core Tenets:** Assumes structural duality consisting of a low-productivity subsistence agricultural sector with unlimited supplies of labor, and a high-productivity urban industrial capitalist sector. Growth occurs as the capitalist sector reinvests its profits to absorb surplus labor from agriculture at a constant institutional wage.
- Expectations:** Structural transformation occurs naturally as labor moves to higher-productivity industrial sectors, accelerating urbanization and raising national savings rates.
- Weaknesses:** Assumes industrial profits are automatically reinvested domestically rather than counterfeited into speculative real estate or expatriated abroad. It also overlooks the risk of

premature urban migration outstripping industrial job creation, which simply shifts rural poverty into expanding urban informal slums (Etim and Edet, 2021).

#### 4.4.2 Stages of Economic Growth (Rostow, 1960)

- **Core Tenets:** Posits that all societies progress through five linear historical stages: traditional society, preconditions for take-off, take-off, drive to maturity, and age of high mass consumption.
- **Expectations:** Targeted policy interventions can help an economy transition from one stage to the next by forcing national savings and investment rates past a critical threshold (typically  $\geq 10\%$  of GDP).
- **Weaknesses:** This rigid, linear model reflects a highly Western-centric developmental path. It assumes that historic conditions can be effortlessly replicated across different eras, completely ignoring how modern global structural inequalities trap developing countries in low-value primary commodity roles (Amadou *et al.*, 2020).

#### 4.4.3 Harrod-Domar Growth Model

- **Core Tenets:** Focuses on the dual nature of investment, which simultaneously creates demand and expands productive capacity. The growth rate ( $g$ ) is determined by the national savings rate ( $s$ ) divided by the incremental capital-output ratio ( $c$ ), expressed as:

$$g = \frac{s}{c}$$

- **Expectations:** Policymakers can hit a target growth rate simply by adjusting the domestic savings rate or by using foreign aid and external loans to bridge any "savings gap."
- **Weaknesses:** The model assumes fixed production coefficients and zero

substitutability between capital and labor. This rigidity leads to a highly unstable "knife-edge" equilibrium where even a minor slip from the warranted growth path triggers persistent unemployment or chronic inflation.

#### 4.4.4 Neoclassical Growth Model (Solow-Swan, 1956)

- **Core Tenets:** Introduces a production function with substitutable factors (capital and labor) and diminishing marginal returns to capital. The model is expressed as:

$$Y = AF(K, L)$$

Long-run per capita growth is determined entirely by exogenous technological progress ( $A$ ).

- **Expectations:** Higher savings rates only temporarily accelerate growth during the transitional phase toward a steady state. Over the long run, economies automatically converge toward a steady-state growth rate driven by population growth and technological advancement.
- **Weaknesses:** Treating technological progress ( $A$ ) as an exogenous parameter leaves the primary driver of long-run growth unexplained within the model itself ("a black box"). The assumption of automatic cross-country income convergence is also frequently disproven by persistent, widening global income gaps (Acemoglu, 2020).

#### 4.4.5 Endogenous Growth Theory (Romer, 1986; Lucas, 1988)

- **Core Tenets:** Endogenizes technological progress by modeling it as the direct result of deliberate human capital accumulation, research and development, and knowledge spillovers. By treating knowledge as a non-rival, partially excludable good, the model eliminates the problem of diminishing marginal returns to aggregate capital (Romer, 2020).

- **Expectations:** Macroeconomic policies directly influence long-run steady-state growth rates. Public investments in education, basic scientific research, and infrastructure generate permanent positive externalities that raise long-term output.
- **Weaknesses:** Requires high institutional quality, effective legal protections for intellectual property, and well-developed financial markets to function

successfully. These vital preconditions are often missing or compromised in developing nations (Saheed and Omitola, 2022).

#### 4.5 Comparative Matrix of Key Growth Theories

The following matrix compares the core mechanisms, policy focal points, and limitations across all reviewed theories:

Theory	Core Engine of Growth	Key Macro Policy Tool	Primary Expectation	Fundamental Structural Weakness
<b>Resource-Based Growth</b>	Extraction of natural resource endowments and conversion into physical capital assets.	Sovereign Wealth Funds, sterilization interventions, and structural diversification funds.	Generation of substantial fiscal revenues and foreign exchange to fund industrial infrastructure.	Institutional degradation, Dutch Disease, and vulnerability to global commodity price shocks.
<b>Export-Led Growth</b>	Tapping into global consumer demand and capturing manufacturing economies of scale.	Competitive exchange rates, export subsidies, and establishing Special Economic Zones (SEZs).	Accelerated domestic productivity gains via learning-by-exporting and hard currency accumulation.	Fallacy of composition, long-term terms-of-trade degradation, and high external vulnerability.
<b>Schumpeterian Growth</b>	Disruptive technological innovation driven by the entrepreneur.	R&D fiscal incentives, STEM funding, and specialized innovation credit markets.	Permanent expansions of the productivity frontier via creative destruction.	Assumes highly advanced credit markets and can cause deep structural unemployment during transitions.
<b>Dual-Economy Model</b>	Reinvesting industrial profits to absorb surplus labor from agriculture.	Industrial capital subsidies and managed wage policies.	Smooth, structural transformation from agrarian economies to	Overlooks the risk of premature urban migration and assuming automatic

Theory	Core Engine of Growth	Key Macro Policy Tool	Primary Expectation	Fundamental Structural Weakness
			urbanized industrial systems.	domestic profit reinvestment.
<b>Stages of Growth</b>	Capital accumulation driving progression through linear developmental steps.	Increasing domestic savings rates past fixed GDP thresholds.	Automatic progression toward modern, high mass-consumption economic status.	Employs a rigid, Western-centric perspective that ignores modern global trade barriers.
<b>Harrod-Domar Model</b>	Aggregate savings and investment efficiencies.	Foreign aid injection and fiscal policies to close the national "savings gap."	Linear, direct relationship between capital investment volume and output growth.	Knife-edge stability risk and assuming fixed production coefficients for labor and capital.
<b>Neoclassical Model</b>	Exogenous technological progress and transitional capital accumulation.	Promoting long-term price stability to optimize private capital deepening.	Automatic convergence toward a steady-state growth path across nations.	Leaves the primary engine of long-run growth (technological progress) unexplained as an exogenous factor.
<b>Endogenous Growth</b>	Human capital accumulation, knowledge spillovers, and domestic R&D.	Public investments in education, digital infrastructure, and innovation systems.	Permanent increases in the long-run growth rate through targeted public policy.	Assumes high institutional capacity and well-developed intellectual property rights.

## 5. Bridging the Gap: The Theoretical-Empirical Disconnect in Developing Economies

The structural mismatch between growth theory predictions and real-world outcomes in developing nations like Nigeria is driven by several deep-seated economic distortions:

### 5.1 Institutional Weaknesses and Rent-Seeking Behaviour

Standard growth models assume a friction-free institutional environment where property rights are secure, the rule of law is absolute, and corruption is non-existent. In reality, large resource rents or targeted industrial subsidies

often encourage rent-seeking rather than productive investment. Macroeconomic policies regularly fail when weak institutions allow public funds to be redirected away from infrastructure and human capital toward political patronage networks.

### 5.2 Financial Market Fragmentation

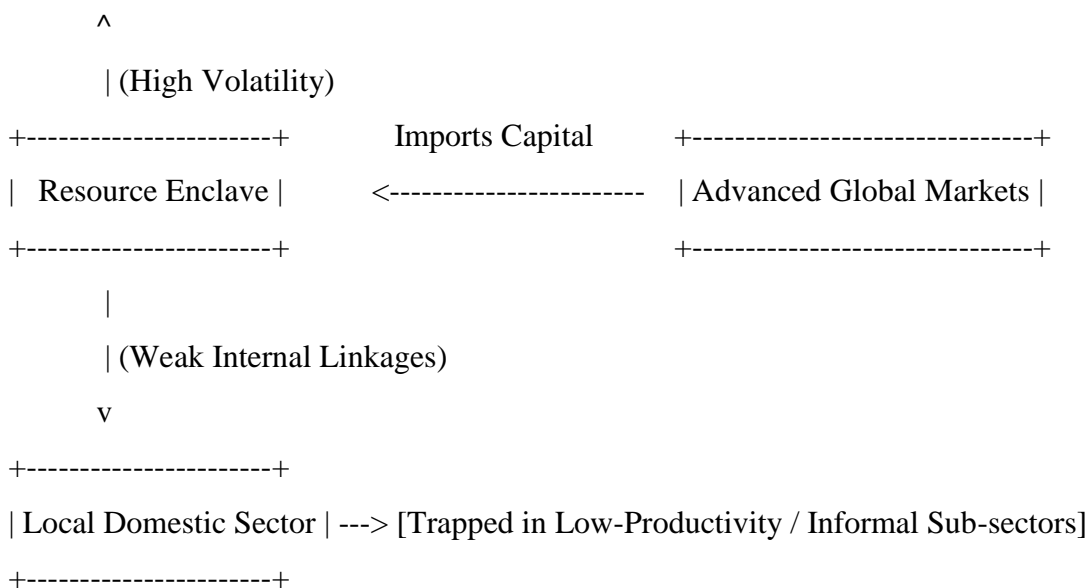
Models like the Schumpeterian and Endogenous growth frameworks rely on deep, efficient financial systems capable of smoothly converting domestic savings into long-term industrial and innovative credit. However, developing economies are often plagued by highly fragmented financial sectors. High commercial lending rates, brief loan maturities, and massive public debt issuance crowd out

private sector borrowing. As a result, credit flows toward short-term import financing and low-risk government securities rather than high-impact capital formation.

### 5.3 Missing Domestic Value Chains

Export-led and dual-economy models assume that expanding industrial production creates strong internal economic linkages. In many developing countries, manufacturing and resource extraction operate as isolated economic enclaves. These sectors import their high-tech inputs and export raw or minimally processed goods, generating few local employment opportunities or technological spillovers for the broader domestic economy.

[Global Raw Material Demand]



### 5.4 Balance of Payments Constraints and Thirlwall's Law

While neoclassical models assume that capital flows automatically to developing nations to maximize returns, real-world growth is aggressively constrained by balance-of-

payments considerations. Thirlwall's Law demonstrates that a country's long-run growth rate cannot exceed the rate consistent with a balanced current account. Developing nations with a high-income elasticity of demand for advanced imports relative to foreign demand for

their primary exports face persistent balance-of-payments barriers whenever they attempt to accelerate growth.

## 6. Conclusion and Policy Recommendations

### 6.1 Conclusion

This paper demonstrates that while foundational and contemporary growth theories offer valuable conceptual insights, their direct translation into macroeconomic policy often fails in developing economies due to unrealistic assumptions. No single growth model provides a flawless roadmap for sustainable development. Resource-based models risk inducing Dutch Disease and institutional vulnerability; export-led strategies face trade barriers and terms-of-trade degradation; and Schumpeterian and endogenous growth models are constrained by financial fragmentation and institutional capacity gaps.

The persistent gaps between theoretical expectations and empirical outcomes—such as Nigeria’s recent growth volatility despite high global oil prices—highlight the need to move past passive stabilization policies. Instead, nations must design holistic macroeconomic frameworks that actively address structural rigidities, build domestic institutional capacity, diversify the economic base, and foster human capital accumulation.

### 6.2 Policy Recommendations

To construct a more effective, structurally grounded macroeconomic policy framework, developing nations should implement the following targeted interventions:

1. **Implement Countercyclical Fiscal Rules:** Establish strict, legally insulated fiscal rules alongside Sovereign Wealth Funds to manage volatile commodity revenues. Governments should save surplus income during resource booms to provide stability during market downturns, keeping public infrastructure investments consistent.
2. **Deploy Targeted, Credit-Directing Monetary Policies:** Central banks

should transition away from blunt, hyper-restrictive interest rates that crowd out private investment. Instead, they should deploy targeted credit interventions, credit guarantees, and development banking windows to support domestic manufacturing, agrotechnology, and innovative start-ups.

3. **Build Deep Industrial Linkages via Integrated SEZs:** Shift from simple raw material exportation to localized value addition by establishing Special Economic Zones (SEZs). These zones should require foreign investments to integrate with local suppliers, encouraging domestic technology transfers and building robust internal value chains.
4. **Prioritize Human Capital and Digital Infrastructure:** In line with endogenous growth principles, fiscal policy must prioritize long-term investments in STEM education, technical vocational training, and digital infrastructure. Enhancing human capital increases total factor productivity and equips the domestic workforce to adapt and innovate.
5. **Maintain a Balanced, Competitive Exchange Rate Regime:** Avoid overvaluing the national currency during resource booms. Central banks should maintain a balanced, predictable real effective exchange rate to shield domestic agriculture and manufacturing from Dutch Disease, keeping exports structurally competitive in regional and global markets.

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